STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

WISCONSIN ENERGY CORPORATION, INTEGRYS ENERGY GROUP, INC., PEOPLES ENERGY, LLC, THE PEOPLES GAS LIGHT AND COKE COMPANY, NORTH SHORE GAS COMPANY, ATC MANAGEMENT INC., and AMERICAN TRANSMISSION COMPANY LLC	)	
Application pursuant to Section 7-204 of the Public Utilities Act for authority to engage in a Reorganization, to enter into agreements with affiliated interests pursuant to Section 7-101, and for such other approvals as may be required under the Public Utilities Act to effectuate the Reorganization.	)	Docket No. 14-0496

Rebuttal Testimony of

SCOTT J. LAUBER

Vice President and Treasurer –
Wisconsin Energy Corporation

On Behalf of
Wisconsin Energy Corporation

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I. INTRODUCTION AND BACKGROUND

A. Witness Identification

Q. Please state your name and business address.

A. My name is Scott J. Lauber. My business address is Wisconsin Energy Corporation ("Wisconsin Energy"), 231 West Michigan Street, Milwaukee, Wisconsin 53203.

Q. Are you the same Scott J. Lauber who provided direct and supplemental direct testimony on behalf of Wisconsin Energy in this docket?

A. Yes.

B. Purpose of Rebuttal Testimony

Q. What is the purpose of your rebuttal testimony in this proceeding?

A. My rebuttal testimony responds to the direct testimony of Illinois Commerce Commission ("Commission" or "ICC") Staff witnesses Eric Lounsberry, Daniel G. Kahle, Dianna Hathhorn and Michael McNally, City of Chicago ("City") and Citizens Utility Board ("CUB") (collectively, "City/CUB") witness Michael P. Gorman, and Retail Energy Supply Association ("RESA") witness Joseph Clark.

C. Summary of Conclusions

Q. Please summarize the conclusions of your rebuttal testimony.

A. In my rebuttal testimony, I conclude:

(1) In response to Staff witness Eric Lounsberry's recommendation as to additional information that could be provided to support the Commission finding that the proposed Reorganization meets the requirements of Section 7-204(b)(1) of the Public

Utilities Act (the "Act"), the Joint Applicants provide commitments with respect to the capital expenditures of Peoples Gas and North Shore.

(2) City/CUB witness Michael Gorman's proposal that the Joint Applicants commit to ring-fence protections for the capital investments of the Gas Companies with respect to dividend payment obligations is unnecessary in light of existing protections under Section 7-103 of the Act and the Joint Applicants' commitments with respect to capital expenditures made in response to Mr. Lounsberry's recommendation.

(3) The Joint Applicants agree with Staff witness Ms. Hathhorn's plan with respect to approving the proposed WEC Energy Group Affiliated Interest Agreement ("AIA") on an interim basis to allow the Commission to find that the proposed Reorganization meets the requirements of Sections 7-204(b)(2) and 7-204(b)(3) of the Act, and agree to accept the conditions she proposed in furtherance of that plan. The Joint Applicants, however, cannot at this time provide an update to their proposed WEC Energy Group AIA with changes acceptable to the Joint Applicants from Docket Nos. 12-0273/13-0612 (Consol.) because open issues concerning the proposed terms in that proceeding need to be resolved first.

(4) The proposed Reorganization meets the requirements of Section 7-204(b)(4) of the Act, as concluded by Staff witness Michael McNally.

(5) The Joint Applicants disagree with Staff witness Mr. McNally's conclusion that the Commission cannot make the finding required by Section 7-204(b)(7) of the Act without imposing conditions on its approval of the Reorganization. The Joint Applicants respectfully conclude that Mr. McNally's position is based on hypothetical scenarios that "possibly" could occur, and thus do not meet Section 7-204(b)(7)'s

standard of adverse rate impacts being "likely" to occur. In an effort to obtain Staff's agreement that the requirements of Section 7-204(b)(7) have been met, however, the Joint Applicants agree to accept certain conditions designed to address Mr. McNally's concerns. To the extent possible, where the Joint Applicants cannot agree to accept the terms of conditions as Mr. McNally proposed them, the Joint Applicants propose a clarification or alternative condition.

(6) The proposed Reorganization meets the requirements of Section 7-204(b)(4) of the Act, as concluded by Staff witness Daniel Kahle.

(7) In response to commitments proposed by City-CUB witness Mr. Gorman, the Joint Applicants agree not to seek recovery of severance costs or early termination fees that are "transaction" costs because they are incurred as part of accomplishing the proposed Reorganization (*i.e.* executive change-in-control payments identified in SEC Form S-4), but reserve the right to recover normal "transition" costs, including future severance costs incurred to create efficiencies and savings.

(8) Based on recent changes made by the Financial Accounting Standards Board and the U.S. Securities Exchange Commission ("SEC"), the Joint Applicants no longer need to seek an exception from the SEC to opt not to follow push-down accounting for the books and financial statements of the Gas Companies with respect to the Reorganization. Accordingly, the Joint Applicants agree to accept conditions with respect to push-down accounting proposed by Staff witness Mr. Kahle after they have been modified to reflect the fact that an exception is no longer needed from the SEC, but conclude that the condition proposed by Mr. Kahle requiring updates on the status of an exception from push-down accounting sought from the SEC is no longer necessary.

(9) While the Joint Applicants do not agree with Mr. McNally that Section 6-103 of the Act must be addressed by the Commission to approve the proposed Reorganization based on the express language of Section 7-204(e) of the Act, the Joint Applicants agree to accept a condition proposed by Staff witness Mr. McNally – for which the joint Applicants propose language – requiring the filing of a compliance report describing the Gas Companies' post-merger capital structures and identifying adjustments, if any, resulting from the merger. The Joint Applicants further agree that in the event they do make push-down accounting adjustments to the Gas Companies' balance sheets as a result of the Reorganization, they will file a petition for approval of the fair value studies and resulting capital structures for the Gas Companies pursuant to Section 6-103.

(10) The Joint Applicants disagree that Section 9-230 is applicable to a proceeding under Section 7-204 of the Act for approval of a proposed reorganization, and conclude that the issues Mr. McNally is concerned about with respect to Section 9-230, which are only hypothetical at the present time, can be addressed when the Gas Companies file for their next rate case if they do materialize. Moreover, Mr. McNally's proposed study of the Gas Companies' capital structures similar to those required by the Commission for Commonwealth Edison Company and Ameren Illinois Company in connection with their formula rate cases is unnecessary, both because of the speculative nature of his concerns and the difference in circumstances between the present Reorganization and the changes brought on by legislative formula rates.

(11) While reserving the right to seek appropriate regulatory and legal changes that may be required, the Joint Applicants commit to maintaining the Gas Companies'

existing large volume transportation and small volume Choices For You programs in substantially the same form as they exist now, in response to a request by RESA. Further, the Joint Applicants commit to honor the commitments made in their pending rate cases with respect to obtaining a purchase of receivables tariff and to reinstate the intraday nomination pilot provision in Rider P which expired on January 31, 2014. With respect to the other proposals suggested by RESA, the Joint Applicants propose working with RESA on a stipulation or other agreement to memorialize the Joint Applicants' commitment to address these issues with RESA after the close of the Reorganization.

D. Itemized Attachments to Rebuttal Testimony

Q. Are you sponsoring any exhibits with your rebuttal testimony?

A. No.

II. SECTION 7-204(b)(1) AND CAPITAL EXPENDITURE COMMITMENTS

Q. What are the requirements of Section 7-204(b)(1) under the Act?

A. Section 7-204(b)(1) of the Act requires that before the Commission can approve a reorganization, it must find that "the proposed reorganization will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service."

Q. Will you be addressing the requirements of Section 7-204(b)(1) in this rebuttal testimony?

A. In part. Joint Applicants witness Mr. Allen Leverett addresses the majority of the issues raised by Staff and intervenors with respect to Section 7-204(b)(1) in his rebuttal testimony (Joint Applicants Ex. 6.0). I will address a recommendation made by Staff

witness Mr. Lounsberry in connection with Section 7-204(b)(1) pertaining to capital expenditures.

Q. What recommendation did Mr. Lounsberry make with respect to capital expenditures in connection with Section 7-204(b)(1) in his direct testimony (Staff Ex. 2.0, 30-32)?

A. Mr. Lounsberry testified that the Joint Applicants had not made a commitment with respect to the Gas Companies'[1] post-reorganization level of capital expenditures and opined that failure to maintain sufficient levels of capital expenditure investment could diminish the ability of the Gas Companies to provide adequate, reliable, efficient, safe and least-cost public utility service, and thus the absence of a capital expenditure commitment by the Joint Applicants would be a deficiency in their ability to meet the requirements of Section 7-204(b)(1). Mr. Lounsberry thus recommended that the Joint Applicants make a commitment regarding the Gas Companies' levels of capital expenditure for the years 2015 through 2017.

Q. What is the Joint Applicants' response to Mr. Lounsberry's opinion and recommendation concerning a commitment on capital expenditures?

A. Given the Joint Applicants' commitments to continue Peoples Gas' AMRP and operate the Gas Companies in a seamless fashion after the close of the proposed Reorganization, the Joint Applicants respectfully disagree that the proposed Reorganization will not satisfy the requirements of Section 7-204(b)(1) of the Act. However, in an effort to cooperate in good faith with Staff and obtain Staff's agreement that the proposed

[1] Unless otherwise indicated, capitalized terms in this rebuttal testimony herein have the same meaning as in the witness' direct testimony.

Reorganization has met all the requirements of Section 7-204(b), the Joint Applicants will make additional commitments with respect to future levels of the Gas Companies' capital investments.

Q. What are the Joint Applicants' commitments with respect to future levels of the Gas Companies' capital investments?

A. The Joint Applicants have considered Mr. Lounsberry's recommended format for making a commitment to specific capital expenditure levels for each of the Gas Companies, in each year 2015 through 2017, and, for Peoples Gas, broken down into AMRP and non-AMRP related capital expenditures. Respectfully, the Joint Applicants believe that given the unforeseen circumstances that can occur in a particular year and cause extreme variance in the ability to perform a planned level of capital work, as well as to cause such work to be performed less efficiently and cost-effectively, commitments to spend specific dollar amounts in particular future years would not be the best manner in which to address the concern Mr. Lounsberry has expressed. For example, if the Joint Applicants commit that Peoples Gas will spend a specific dollar amount on AMRP in 2016, severe weather could occur in that year which not only makes it difficult or impossible to perform the planned level of capital investment that year, but also makes it more expensive to perform work in those extreme conditions. In that situation, it may make sense to push the work – and the capital expenditures – into the following year. Having specific capital expenditure commitments for each year would act to prevent such cost effective decisions from being made, to the detriment of customers who would get less value from capital expenditures required to be made under such circumstances.

Accordingly, the Joint Applicants have chosen to make an aggregate commitment to a level of capital expenditures for each of Peoples Gas and North Shore for the three-year period 2015-2017. For Peoples Gas, the Joint Applicants commit that they will make a total of at least $1 billion in capital expenditures (combined AMRP and non-AMRP related) during the 2015-2017 period. For North Shore, the Joint Applicants commit that they will make a total of at least $35 million in capital expenditures during the 2015-2017 period. The Joint Applicants believe this approach combines a commitment to a sufficient level of capital expenditures to demonstrate that the ability of the Gas Companies to provide adequate, reliable, efficient, safe and least-cost public utility service will not be diminished, with the flexibility necessary to ensure that these capital expenditures are made in a prudent and cost-effective manner. Further, if at any time during the 2015-2017 time period the Joint Applicants determine that an issue has arisen concerning whether these levels of capital expenditures will be reached by the end of that time period, the Joint Applicants will consult with Staff to discuss the appropriate steps that should be taken to resolve the issue.

Q. Did any other party address the issue of maintaining the Gas Companies' capital expenditures after the proposed Reorganization is closed?

A. Yes. City/CUB witness Michael Gorman opined that it is a "near certainty" that WEC Energy Group will increase the Gas Companies' dividend payment obligations, and that financial pressures from the reorganization may restrict the amount of internal cash flow available to support utility capital investments. (City/CUB Ex. 4.0, 21:500-504) Mr. Gorman recommended that the Joint Applicants commit to "enforceable ring-fence restrictions" that would limit the ability of the Gas Companies to make dividend

payments or other cash transfers to WEC Energy Group before planned AMRP budgets are fully funded. (City/CUB Ex. 4.0, 22:529-533)

Q. What is the Joint Applicants' response to Mr. Gorman's ring-fence proposal?

A. The Joint Applicants respectfully disagree that any ring-fence provisions are necessary to ensure that the Gas Companies continue to make sufficient capital investments, particularly with respect to Peoples Gas' AMRP. Along with their commitment on the Peoples Gas AMRP (as Joint Applicants witness Mr. Leverett discusses in his direct and rebuttal testimonies, Joint Applicants Exs. 1.0 and 6.0, respectively), the commitments that the Joint Applicants have made above provide adequate assurance that the Gas Companies will continue investing in their infrastructure as is reasonable and appropriate.

With regard to Mr. Gorman's concern that WEC Energy Group might put undue pressure on the Gas Companies to pay dividends at a level that will cause harm to their capital or interfere with their service obligations, the Act already provides protection and empowers the Commission to take action to stop such harm from occurring. Section 7-103(1) of the Act authorizes the Commission to order a public utility to cease and desist the declaration and payment of any dividend if the Commission finds the utility's capital has or would become impaired. Additionally, Section 7-103(2) of the Act prohibits a utility from paying any dividend unless its earnings and earned surplus are sufficient to declare and pay such dividend after provision is made for reasonable and proper reserves, and unless such dividend can be paid "without impairment of the ability of the utility to perform its duty to render reasonable and adequate service at reasonable rates." Thus, for this reason as well, Mr. Gorman's proposed ring-fence commitment is unnecessary.

III. REQUIREMENTS OF SECTIONS 7-204(b)(2) AND 7-204(b)(3)

Q. What are the requirements of Section 7-204(b)(2) under the Act?

A. Section 7-204(b)(2) of the Act requires that before the Commission can approve a reorganization, it must find that the proposed Reorganization "will not result in the unjustified subsidization of non-utility activities by the utility or its customers."

Q. What are the requirements of Section 7-204(b)(3) under the Act?

A. Section 7-204(b)(3) of the Act requires that before the Commission can approve a reorganization, it must find that the "costs and facilities are fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utility for ratemaking purposes."

Q. Has Staff addressed this requirement in direct testimony?

A. Yes. Staff witness Ms. Hathhorn addressed this requirement in her testimony (Staff Ex. 6.0).

Q. What were Ms. Hathhorn's conclusions and recommendations with respect to the requirements of Sections 7-204(b)(2) and 7-204(b)(3)?

A. In light of the open proceeding (Docket Nos. 12-0273/13-0612 (Consol.)) in which the Commission is investigating certain issues with respect to Integrys' current Affiliated Interest Agreement that was approved in Docket No. 10-0408 (the "10-0408 AIA"), Ms. Hathhorn concluded that the Commission should not, at this time, approve the Joint Applicants' proposed WEC Energy Group Affiliated Interest Agreement (Joint Applicants Ex. 2.4), which is based upon the 10-0408 AIA, at this time. However, to

allow the Commission to find that the proposed Reorganization meets the requirements of Sections 7-204(b)(2) and 7-204(b)(3), Ms. Hathhorn proposed a plan whereby the Commission will approve the WEC Energy Group AIA on an interim basis until the Commission has approved a new affiliated interest agreement in an order issued in Docket Nos. 12-0273/13-0612 (Consol.), which would then become the governing document for affiliate transactions between the Joint Applicants. Ms. Hathhorn concluded that with these actions, the Commission should find that the proposed Reorganization meets the requirements of Sections 7-204(b)(2) and 7-204(b)(3).

Q. Do the Joint Applicants agree with Ms. Hathhorn's proposed plan?

A. Yes. Accordingly, the Joint Applicants agree to accept conditions (1) and (2) set forth on page 11 of Ms. Hathhorn's direct testimony (Staff Ex. 6.0, 11:248-258).

Q. Ms. Hathhorn recommended that the Joint Applicants update their proposed WEC Energy Group AIA with their rebuttal testimony to reflect any of the changes proposed by Staff to the 10-0408 AIA that are acceptable to the Joint Applicants (Staff Ex. 6.0, 6:122-124). Do the Joint Applicants have any such updates at this time?

A. At the present time, discovery is ongoing in Docket Nos. 12-0273/13-0612 (Consol.) between Staff and the Gas Companies concerning the changes proposed by Staff to the 10-0408 AIA that the Joint Applicants believe needs to be resolved before they can provide an update to the proposed WEC Energy Group AIA in this proceeding.

Q. In connection with Sections 7-204(b)(2) and 7-204(b)(3), Ms. Hathhorn also recommended a condition requiring that the Gas Companies supplement the

information they provide annually in their Form 21 ILCCs to the Commission, beginning with the 2014 information to be submitted by March 31, 2015 (Staff Ex. 6.0, 9:190-207). What is the Joint Applicants' response to this recommended condition?

A. The Joint Applicants agree to accept this condition as it is stated on pages 11-12 of Ms. Hathhorn's direct testimony (Staff Ex. 6.0, 11:259 – 12:273).

Q. Has any other party addressed the requirements of Section 7-204(b)(2) and 7-204(b)(3) in direct testimony?

A. No.

IV. REQUIREMENTS OF SECTION 7-204(b)(4)

Q. What are the requirements of Section 7-204(b)(4) under the Act?

A. Section 7-204(b)(4) of the Act requires that before it can approve a proposed reorganization, the Commission must find that "the proposed reorganization will not significantly impair the utility's ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure."

Q. Has Staff addressed this requirement in direct testimony?

A. Yes. Staff witness Michael McNally addressed this requirement on pages 3-8 of his direct testimony (Staff Ex. 7.0). Mr. McNally concluded that the Joint Applicants have met the requirement of Section 7-204(b)(4) of the Act (Staff Ex. 7.0, 8:163-173).

Q. Has any other party addressed this requirement in direct testimony?

A. No.

V. REQUIREMENTS OF SECTION 7-204(b)(7)

Q. What are the requirements of Section 7-204(b)(7) under the Act?

A. Section 7-204(b)(7) of the Act requires that before it can approve a proposed reorganization, the Commission must find that "the proposed reorganization is not likely to result in any adverse rate impacts on retail customers."

Q. Has Staff addressed this requirement in direct testimony?

A. Yes. Staff witness Michael McNally addressed this requirement on pages 8-12 of his direct testimony (Staff Ex. 7.0). Significantly, Mr. McNally did not conclude that it is "likely" that the proposed Reorganization would result in an adverse rate impact on customers. Rather, Mr. McNally testified that it is "possible" that the Gas Companies rates might be higher. Mr. McNally based this conclusion of a "possible" rate increase on a hypothetical scenario involving the following: a credit downgrade might occur due to the debt incurred to finance Wisconsin Energy's acquisition of Integrys' stock; lower credit ratings might result in higher debt costs; higher debt costs might lead to higher costs of capital; higher costs of capital might result in higher rates. Based on that theoretical risk, Mr. McNally recommended that the Commission impose the following five conditions on its approval of the proposed Reorganization:

- Require the Gas Companies to maintain separate credit facilities, not accessible to nor influenced by non-utility affiliates;
- Prohibit the Gas Companies from lending to non-utility affiliates under Section 7-101 of the Act or Illinois Administrative Code Part 340;
- Prohibit the Gas Companies from guaranteeing any obligations of their non-utility

affiliates;

- Require Wisconsin Energy to notify the Commission before increasing its proportion of non-regulated operations and indebtedness; and

- Require the Gas Companies to register with the SEC or to present a detailed study showing costs and savings of registration compared to remaining unregistered.

Q. What is the Joint Applicants' response to Mr. McNally's conclusions and proposed conditions?

A. As an initial matter, the Joint Applicants have made a commitment not to increase base rates for a period of two years from the close of the Transaction, as explained in Mr. Leverett's direct testimony. (Joint Applicants Ex. 1.0 at 21:452-61) As a starting point for evaluating this issue, that commitment should be recognized, though it does not appear to be considered by Mr. McNally.

Even putting that commitment aside, the Joint Applicants respectfully disagree with Mr. McNally's conclusion that the Commission cannot make the finding required by Section 7-204(b)(7) without imposing additional conditions on its approval of the proposed Reorganization. Mr. McNally's testimony is careful to couch the scenario that would result in a rate increase as possible (*i.e.*, theoretical), but not likely. Indeed, in response to a question about whether the Gas Companies' costs of capital are likely to increase as a result of the proposed reorganization, he specifically states: "I do not know if it is likely, but it is certainly possible." (ICC Staff Ex. 7.0 at 9:183-85) The standard contained in Section 7-204(b)(7) is whether adverse rate impacts are "likely" to occur, not whether under any hypothetical scenario they are "possible."

Nevertheless, in an effort to obtain Staff's agreement that the requirements of Section 7-204(b) have been met for the proposed Reorganization, the Joint Applicants have evaluated the conditions that Mr. McNally proposed and have considered the extent to which they can agree to those conditions. The Joint Applicants' positions on the proposed conditions address the concerns Mr. McNally expressed, and should allow him to recommend that the Commission find that the requirements of Section 7-204(b)(7) have been met. The Joint Applicants' position with respect to each proposed condition is addressed individually, below.

Q. What is the Joint Applicants' position with respect to Mr. McNally's proposed condition to require that Peoples Gas and North Shore are to maintain separate credit facilities, not accessible to nor influenced by non-utility affiliates (Staff Ex. 7.0, 10:234-235)?

A. The Joint Applicants do not oppose a condition of this nature, but propose that the condition be amended to reflect that Peoples Gas and North Shore should maintain any separate credit facilities to the extent they existed prior to approval of the proposed Reorganization. This amendment is necessary to reflect the fact that North Shore currently does not have its own separate credit facility, but is able to borrow from Peoples Gas and the Integrys holding company under inter-company loan agreements approved by the Commission in Docket Nos. 04-0602 and 04-0603 (as amended in Docket Nos. 10-0588 and 12-0284). With this clarification, the Joint Applicants agree to accept this proposed condition.

Q. What is the Joint Applicants' position with respect to Mr. McNally's proposed condition to prohibit Peoples Gas and North Shore from lending to non-utility

affiliates under Section 7-101 of the Act or 83 Illinois Administrative Code Part 340 (Staff Ex. 7.0, 11:236-238)?

A. The Joint Applicants agree to accept this proposed condition.

Q. What is the Joint Applicants' position with respect to Mr. McNally's proposed condition to prohibit Peoples Gas and North Shore from guaranteeing any obligations of their non-utility affiliates (Staff Ex. 7.0, 11:239-240)?

A. The Joint Applicants agree to accept this proposed condition.

Q. What is the Joint Applicants' position with respect to Mr. McNally's proposed condition that would require Wisconsin Energy to notify the Commission before increasing its proportion of non-regulated operations and indebtedness (Staff Ex. 7.0, 11:241-242)?

A. The Joint Applicants respectfully cannot agree to this condition. The terms of this condition are simply too broad and it would be unnecessarily burdensome. The proposed condition creates the potential for inappropriate micromanagement of the Gas Companies' holding company by the Commission. Further, this condition is unnecessary because under the Act, the Commission already is required to approve any non-exempt transaction between a new non-utility affiliate and the Gas Companies, and the Joint Applicants will need to provide notice to the Commission if they add such an affiliate to the proposed WEC Energy Group AIA. Also, under the Wisconsin Utility Holding Company Act, WI Stat § 196.795(7), the Public Service Commission of Wisconsin conducts an audit of the WEC Energy Group and its subsidiaries every three years, which includes a review of affiliates and affiliate transactions. To further address the concern Mr. McNally seeks to address with this proposed condition, the Joint Applicants propose

instead that the Commission add a condition requiring the filing with the Commission of the reports of those investigations required under the Wisconsin Utility Holding Company Act, which will keep the Commission informed about the Gas Companies' holding company parent and affiliates on a regular and ongoing basis.

Q. What is the Joint Applicants' position with respect to Mr. McNally's proposed condition that would require Peoples Gas and North Shore to register with the SEC or to present a detailed study showing costs and savings of registration compared to remaining unregistered (Staff Ex. 7.0, 11:243-246)?

A. As explained in my supplemental direct testimony (Joint Applicants Ex. 5.0, 4:82-90), it would not be cost effective for Peoples Gas and North Shore to become registrants with the SEC. Indeed, it is my understanding that both of the Gas Companies were previously registrants with the SEC but terminated their registrations because there was no advantage to issuing SEC-registered debt in the public markets given the relatively small size of their debt issuances (*i.e.*, below $250 million).[2] This decision has allowed the Gas Companies to save on SEC, audit and accounting fees associated with being SEC-listed companies, while still allowing the Gas Companies access to capital at competitive costs through the private capital markets and through the tax exempt market. Accordingly, the Joint Applicants respectfully disagree with the need either for the Gas Companies to be registered with the SEC or for the presentation of a study on the costs and benefits of registration versus non-registration given the Gas Companies' previous experience with registration, and thus, do not agree to accept this proposed condition.

[2] Peoples Gas and North Shore filed to terminate their registrations with the SEC on January 16, 2008 and September 9, 2010, respectively.

Q. Has any other party provided direct testimony related to the requirements of Section 7-204(b)(7)?

A. Yes. City/CUB witness Mr. Michael Gorman testified that the Joint Applicants' commitment not to seek a change in the Gas Companies' base rates that would go into effect any earlier than two years from the close of the Transaction should be extended to five years. Also, City/CUB witness Ms. Karen Weigert testified that there should be no increase in the fixed charge portions of the Gas Companies' delivery services rates for the length of the period in which a change in base rates would not be sought. Joint Applicants witness Mr. Leverett responds to these positions in his rebuttal testimony (Joint Applicants Ex. 6.0).

VI. REQUIREMENTS OF SECTION 7-204(c)

Q. What are the requirements of Section 7-204(c) under the Act?

A. Section 7-204(c) of the Act requires that before it can approve a proposed reorganization, the Commission must rule on (i) the allocation of any savings resulting from the proposed reorganization; and (ii) whether the companies should be allowed to recover any costs incurred in accomplishing the proposed reorganization and, if so, the amount of costs eligible for recovery and how the costs will be allocated.

Q. Has Staff addressed these requirements in direct testimony?

A. Yes. Staff witness Mr. Kahle addressed these requirements on pages 2-4 of his direct testimony (Staff Ex. 5.0). Mr. Kahle concluded that the proposed Reorganization complies with these requirements.

Q. Mr. Kahle recommended that the Commission make findings that: "Allocation of any savings resulting from the proposed reorganization shall flow through to ratepayers"; and "Any costs incurred in accomplishing the proposed reorganization shall not be recoverable from ratepayers." (Staff Ex. 5.0, 6:120-125) Do the Joint Applicants agree with Mr. Kahle's proposed findings?

A. Yes, with the understanding that the phrase "costs incurred in accomplishing the proposed reorganization" in the second finding refers to "transaction costs" and not "transition costs." "Transaction costs" are the costs associated with executing the transaction at issue, such as banker's fees, legal fees, or severance costs incurred as a result of the transaction (*i.e.*, executive change-in-control payments as identified in an SEC Form S-4). In contrast, "transition costs" are costs incurred after the close of the transaction to achieve long-term efficiencies and savings, and which may be recoverable to the extent they produce savings. Accordingly, the first finding Mr. Kahle recommended in his testimony reflects the fact that the Gas Companies' future rates will reflect savings that are achieved through these transition costs, which may be recovered to the extent they do not exceed the savings they produce. As Joint Applicants witness Mr. Reed testified in his direct testimony (Joint Applicants Ex. 3.0), the savings likely will not exceed the transition costs incurred to produce those savings until five to ten years after the close of the proposed Reorganization.

Q. What is the Joint Applicants' position with respect to Mr. Kahle's proposed condition requiring the Gas Companies in future rate cases to identify all costs included in the test period resulting from accomplishing the reorganization and

demonstrate that such costs are not included in the rate case for recovery (Staff Ex. 5.0, 6:130-132)?

A. The Joint Applicants agree to accept this condition, with the understanding that, as explained in my previous answer above, the costs being referred to are "transaction costs."

Q. Has any other party addressed the issue of how Reorganization costs should be treated in direct testimony?

A. Yes. City/CUB witness Mr. Gorman (City/CUB Ex. 4.0, 11:259-261) requested that the Commission specifically state that any executive, Board of Director or senior employee severance costs or early termination fees related to the proposed Reorganization should not be subject to recovery from retail customers. Further, while it is not clear from his testimony, Mr. Gorman also appears to be asking for the Joint Applicants to voluntarily commit not to recover any post-merger integration costs (*see* City/CUB Ex. 5.0, 25:591-597).

Q. What is the Joint Applicants' response to Mr. Gorman's direct testimony concerning the treatment of costs from the proposed Reorganization?

A. Mr. Gorman's testimony on this issue appears to treat transaction costs and transition costs interchangeably and suggests they be treated the same, which would not be appropriate. With respect to the treatment of executive, Board of Director or senior employee severance costs or early termination fees that are transaction costs because they are incurred as part of accomplishing the proposed Reorganization (*i.e.* the executive change-in-control payments identified in the Form S-4 filed with the SEC in connection with the Transaction), the Joint Applicants agree that these costs will not be recoverable

in rates. However, to the extent Mr. Gorman is asking either for a Commission-imposed condition or voluntary commitment by the Joint Applicants to not recover future severance package costs or other costs incurred to achieve long-term efficiencies and savings, the Joint Applicants respectfully disagree. Future severance package costs which may be incurred to create efficiencies and savings would be properly classified as transition costs. As I discuss above, such transition costs should be recoverable by the Gas Companies to the extent they do not exceed the savings they produce. Joint Applicants witness John J. Reed further explains the Joint Applicants' position on this issue in his rebuttal testimony (Joint Applicants Ex. 8.0).

VII. PURCHASE ACCOUNTING ENTRIES AND THE REQUIREMENTS OF SECTIONS 6-103 AND 9-230

Q. Has any party submitted direct testimony with respect to the Joint Applicants' position that they do not, at this time, need to provide accounting entries to record the reorganization because they expect to meet an exception to push-down accounting, so as not to reflect the impact of the acquisition on the books and financial statements of the Gas Companies?

A. Yes. Staff witness Mr. Kahle addressed this issue on pages 4-6 of his direct testimony (Staff Ex. 5.0). Mr. Kahle agreed with the Joint Applicants' position, but noted that the Joint Applicants have not yet received an exception to push-down accounting from the SEC. He therefore recommended that the Joint Applicants provide updates as to the status of such a request in rebuttal, surrebuttal and late-filed exhibits. Mr. Kahle proposed two conditions concerning actions to be taken with respect to the request for an exception to push down accounting (Staff Ex. 5.0, 7:133-143).

Q. What is your response to Mr. Kahle's request for an update on the status of seeking an exception to push down accounting from the SEC and his two proposed conditions concerning the same?

A. There have been recent changes made by the Financial Accounting Standards Board ("FASB") and the SEC concerning the ability of public and nonpublic companies to opt not to apply push-down accounting without first needing to obtain an exception from the SEC. In November 2014, the FASB issued guidance in the form of Accounting Standards Update No. 2014-17, Business Combinations (Topic 805). This guidance provides public and nonpublic companies with the option of applying pushdown accounting. Concurrent with this guidance, the SEC staff rescinded Staff Accounting Bulletin ("SAB") topic 5.J regarding pushdown accounting. Based on these actions of the FASB and the SEC staff, the Joint Applicants do not require an SEC exception for push-down accounting, and the Joint Applicants will not follow push-down accounting for the Gas Companies. Thus, the Gas Companies' books and records will be carried over at historical cost.

Q. Does this development concerning the FASB and SEC positions on the need to obtain an exception to push-down accounting have any impact on the two conditions Mr. Kahle proposed with respect to push-down accounting on page 7 of his direct testimony (Staff Ex. 5.0, 7:133-143)?

A. Yes. The language of the first proposed condition should be changed to reflect the fact that the Joint Applicants no longer need to apply and receive an exception from the SEC to opt not to apply push-down accounting. The Joint Applicants propose that Mr. Kahle's first proposed condition on push-down accounting be revised to read as follows:

> Should the Joint Applicants opt to follow push-down accounting for the Reorganization, any accounting entries made to the books of the Gas Companies for push-down accounting related to the Reorganization shall be disregarded for ratemaking and regulatory reporting purposes.

Mr. Kahle's second proposed condition concerned filing the determination of its request for an exception to push-down accounting from the SEC. Because a request for an exception to push-down accounting no longer needs to be obtained from the SEC, this condition is no longer necessary.

Q. Did any other Staff witness address the issues of purchase accounting adjustments and push-down accounting?

A. Yes. Staff witness Mr. McNally addressed purchase accounting adjustments and the exception sought for push-down accounting in the context of the requirements of Section 6-103 of the Act on pages 12-15 of his testimony (Staff Ex. 7.0). Section 6-103 of the Act requires that in any reorganization, the Commission shall authorize the amount of capitalization of a public utility formed by a reorganization, which shall not exceed the fair value of the property involved. Mr. McNally concluded that if an exception to push-down accounting is not received from the SEC, and the Gas Companies have accounting adjustments on their balance sheets following the proposed Reorganization, then the Commission would have to act to determine whether the post-merger capitalization of the Gas Companies satisfies the requirements of Section 6-103. If there are no purchase accounting adjustments, then the Gas Companies' capitalization would equal original cost and Section 6-103 would be satisfied. Mr. McNally proposed a condition to require the Gas Companies to file a compliance report describing their post-merger capital structures, with conditional actions to be taken if push-down accounting adjustments to the Gas Companies' balance sheets are made.

Q. What is the Joint Applicants' response to Mr. McNally's testimony on Section 6-103 and his proposed condition?

A. The Joint Applicants respectfully disagree with Mr. McNally's conclusion that Section 6-103 of the Act needs to be addressed for purposes of approving the proposed Reorganization. Section 7-204(e) of the Act provides that "[n]o other Commission approvals shall be required for mergers that are subject to" Section 7-204. Mr. McNally's testimony also does not reflect the developments discussed above concerning the FASB's and SEC's change in position concerning the elimination of the need to obtain an exception to push-down accounting. The Joint Applicants, however, will not oppose a condition as proposed by Mr. McNally on page 15 of his direct testimony (Staff Ex. 7.0, 15:350-360), and propose the following language for the condition:

> The Gas Companies shall file a compliance report in Docket No. 14-0496 within 180 days after the close of the Reorganization, with a copy to the Manager of the Commission's Finance Department, that describes the Gas Companies' post-merger capital structures and identifies capital structure adjustments, if any, that resulted from the Reorganization. In the event that there are push-down accounting adjustments made to the Gas Companies' balance sheets as a result of the Reorganization, then the Gas Companies shall file a petition with the Commission seeking Commission approval of the fair value studies and resulting capital structures for the Gas Companies pursuant to Section 6-103 of the Act.

Q. Mr. McNally also discussed whether the proposed Reorganization would "satisfy the requirement set forth in Section 9-230 of the Act," and concluded that it would be "unlikely." (Staff Ex. 7.0, 15:361 – 16:378) What is the Joint Applicants' response to Mr. McNally's testimony regarding Section 9-230 of the Act?

A. While the Joint Applicants want to work with Staff and reach agreement where possible on areas of concern they have with respect to the proposed Reorganization, the Joint

Applicants respectfully disagree that Section 9-230 of the Act applies to this proceeding and the Commission's approval of the proposed Reorganization. Section 9-230 requires that the Commission not include any incremental risk or increased cost of capital when determining a public utility's rates or charges which is the direct or indirect result of the utility's affiliation with unregulated or nonutility companies. As discussed above, Section 7-204(e) expressly provides that no other Commission approvals besides what is required by Section 7-204 shall be required for the approval of a proposed reorganization subject to Section 7-204. Further, by its very terms, Section 9-230 only applies in a proceeding where the Commission is "determining a reasonable rate of return upon investment for any public utility in any proceeding to establish rates or charges." 220 ILCS 5/9-230. The present proceeding is not one in which the Commission is establishing rates or charges for the Gas Companies. Indeed, one of the commitments made by the Joint Applicants is that they will not seek any change in base rates that would be effective any earlier than two years after the close of the Transaction. At the present time, it is mere speculation whether the proposed Reorganization could result in a credit downgrade or increased costs of capital for the Gas Companies, or whether the Gas Companies could take full advantage of their debt capacities without jeopardizing their or WEC Energy Group's credit ratings. By the time that the Gas Companies file their next rate cases, these questions will be answered, and the Gas Companies and Staff will be able to readily determine if a Section 9-230 issue exists and, if so, make the appropriate adjustments in the rate case proceedings at that time, as contemplated by the express terms of Section 9-230.

Q. What is the Joint Applicants' position with respect to Mr. McNally's proposed condition that would require "a study of appropriate post-merger capital structures for Peoples Gas and North Shore" similar to those ordered in Docket Nos. 11-0721 and 12-0001, to be commenced no later than six months prior to, and to be presented to the Commission in final form at the time of or before, the filing of the Gas Companies' next rate case (Staff Ex. 7.0, 16:379 – 17:387)?

A. Given the speculative nature of the concerns expressed by Mr. McNally that form the basis for such a study, the Joint Applicants respectfully disagree that the Commission should order the performance of such a study at this time. Furthermore, the proposed Reorganization does not present the Commission with the same type of situation to which it was responding when it ordered Commonwealth Edison Company ("ComEd") and Ameren Illinois Company ("Ameren") to work with Staff to explore more leveraged capital structures and/or an equity cap. In those proceedings (Docket Nos. 11-0721 and 12-0001, respectively), the Commission was responding to the dramatic change in the way rates are set for large electric utilities in Illinois resulting from enactment of Illinois' formula rate law codified in Section 16-108.5 of the Act. Because of the adoption of formula rates for electric utilities, the operating risk for electric utilities was reduced from the levels under which their capital structures evolved, and there no longer would be a link between the rate of return on common equity set by the statutory formula and capital structure. *See In re ComEd*, Docket No. 11-0721 (Order May 29, 2012) at p. 133. Such systematic and structural changes to the Gas Companies' levels of operating risk, the way their rates of return on common equity will be determined, and their relation to the Gas Companies' capital structures simply do not exist with respect to the proposed

Reorganization. Accordingly, the Commission should not adopt this condition proposed by Mr. McNally.

Q. Have witnesses for any other party addressed issues concerning purchase accounting entries, push-down accounting, Section 6-103, and/or Section 9-230?

A. No.

VIII. RESA AND THE GAS COMPANIES' TRANSPORTATION PROGRAMS

Q. In the direct testimony of RESA witness Joseph Clark (RESA Ex. 1.0(R), 5:84 – 7:133), RESA expressed concerns regarding the Joint Applicants' commitment to maintaining the Gas Companies' current small and large volume transportation after the close of the proposed Reorganization. What is the Joint Applicants' response to Mr. Clark's testimony?

A. RESA does not have any reason to be concerned with respect to the Joint Applicants' commitment to maintain the Gas Companies' existing large volume transportation and small volume Choices For You programs. While reserving the right to seek appropriate regulatory and legal changes that may be required for operation of those programs over time, the Joint Applicants are committed to maintaining the Gas Companies' existing large volume transportation and small volume Choices For You programs in substantially the same form as they exist now. Put simply, the Joint Applicants do not plan any change in policy with respect to these programs and would like to work with RESA to further discuss the areas of concern raised in Mr. Clark's direct testimony to see if agreement can be reached on possible improvements to the programs.

Q. What is the Joint Applicants' response to RESA's request that the Joint Applicants confirm the commitment made by the Gas Companies' witness, Ms. Debra Egelhoff, in the Gas Companies pending rate cases concerning a purchase of receivables ("POR") program (RESA Ex. 1.0(R), 7:134 – 8:161)?

A. The Joint Applicants are committed to honoring the commitment made by the Gas Companies in the testimony of Ms. Egelhoff in Docket Nos. 14-0224/12-0225 (Consol.) concerning a POR tariff. Additionally, the Joint Applicants would be willing to memorialize a commitment with RESA to discuss and investigate this issue further.

Q. What is the Joint Applicants' response to RESA's request for the Gas Companies to reinstate the intraday nomination pilot provision in Rider P which expired on January 31, 2014 (RESA Ex. 1.0(R), 8:167 – 9:175)?

A. The Joint Applicants are willing to commit to reinstating the intraday nomination provision in the Gas Companies' Rider P that had existed as a pilot that expired on January 31, 2014. The Joint Applicants can work with RESA on an appropriate stipulation to memorialize the Joint Applicants' commitment on this issue.

Q. Do the Joint Applicants have a general response to the other specific proposals that RESA made with respect to the large volume transportation and Choice programs?

A. Yes. RESA offered proposals with respect to modifying several aspects of the large volume transportation and/or Choice programs:

- Reducing the Gas Companies' pooling charges;
- Developing a process to allow PIPP customers to choose an alternative gas supplier;
- Adopting the use of email, a secure FTP site, or fax for enrollment confirmations;

- Modifying the existing Choices For You Billing Services Agreement to make the liquidated damages provision consistent with that type of agreement;
- Develop a "wallet ready" enrollment process; and
- Allow billing for non-commodity products and services by non-affiliates on utility bills.

These issues need further development and would benefit from further discussion and exchange of information between the Joint Applicants and RESA. For example, the Joint Applicants at the present time need more information concerning what a "wallet ready" enrollment process would look like. Likewise, the Joint Applicants are reviewing and considering what changes should be made to the Choices For You Billing Services Agreement. With respect to PIPP customers, the Joint Applicants could explore with RESA what options exist to prevent customers who enroll with an alternative supplier from being removed by the State from the PIPP program. Accordingly, the Joint Applicants propose working with RESA on a stipulation or other agreement to memorialize the Joint Applicants' commitment to address these issues with RESA after the close of the Reorganization.

IX. CONCLUSION

Q. Does this conclude your rebuttal testimony?

A. Yes.